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TO RUEHC/SECSTATE WASHDC 9009  
INFO RUEATRS/DEPT OF TREASURY WASHINGTON DC  
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RUEHBUL/AMEMBASSY KABUL 9177  
RUEHNE/AMEMBASSY NEW DELHI 3813  
RUEHLO/AMEMBASSY LONDON 8753  
RUEHKP/AMCONSUL KARACHI 0376  
RUEHLH/AMCONSUL LAHORE 6118  
RUEHPW/AMCONSUL PESHAWAR 4929  
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL  
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UNCLAS SECTION 01 OF 02 ISLAMABAD 003104

SENSITIVE  
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SUBJECT: DECREASE IN CONSUMER FINANCE LIKELY TO IMPACT INDUSTRIAL  
PRODUCTION

Summary

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¶1. (SBU) Growth in consumer financing slowed in FY07-08 compared to FY06-07, due to rapidly increasing food and energy costs, coupled with stagnant incomes. These have eroded consumers' ability to pay large loan installments, thereby reducing the demand for new lending. Banking executives report to local media they are confident the consumer finance market will revive once the political situation stabilizes, inflation is brought under control, and the cost of credit is reduced. However, with banks becoming more cautious and consumers more reluctant to borrow, demand is likely to decrease, and lower demand, coupled with higher costs of production, could result in decreased industrial production. End Summary.

Decreasing Consumer Financing

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¶2. (SBU) Consumer finance, including personal loans, mortgages and credit cards, grew by 3 percent in FY 07-08, down from 17 percent growth in FY06-07. In absolute terms, the value of outstanding commercial loans grew by PKR 11 billion (USD 144.7 million) during the previous fiscal year, versus PKR 51 billion (USD 671 million) in the FY06-07. Pakistan's total stock of consumer loans currently stands at PKR 359 billion (USD 4.72 billion). Banking executives reported to local media that the slowdown in consumer finance is due mainly to a rise in the cost of borrowing. The State Bank of Pakistan (SBP) discount rate is currently 13 percent and has been increased four times in the last 14 months. Local commercial banks are reportedly more cautious in approving consumer loans and are actively targeting clients with good credit histories for future business.

Mortgage Lending Increases; Personal and Car Loans Decrease

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¶3. (SBU) The share of personal loans in overall consumer loans dropped to just below 39 percent in FY07-08, from close to 41 percent in FY06-07: PKR 140 billion (USD 1.8421 billion) in FY07-08 from PKR 142 billion (USD 1.8684 billion) in FY06-07. Car loans dipped slightly to PKR 104.99 billion (USD 1.381 billion) from PKR 105.44 billion (USD 1.387 billion), with the percentage of car loans in total consumer loans dropping to 29 percent from over 30 percent. Mortgage loans in FY07-08 rose to PKR 66.55 billion (USD 875.7 million) from PKR 54.67 billion (USD 719.3 million) in FY06-07, with the share of mortgage loans in outstanding consumer loans increasing to 18.5 percent from 15.69 percent. Credit card loans climbed modestly to PKR 44.45 billion (USD 584.9 million) from PKR 42.82

billion (USD 563.4 million) - its share of total consumer loans increasing in FY07-08 to 12.4 percent, as compared to 12.2 percent in FY06-07.

#### State Bank Says Consumer Financing Still Strong

14. (SBU) Rapidly increasing food and energy prices, coupled with stagnant incomes, eroded consumer ability to pay large loan installments, thereby reducing the demand for new lending. However, the State Bank of Pakistan (SBP) said in its FY07-08 third quarter report that the overall quality of the consumer finance had been good, although it had started weakening somewhat in 2006. It noted that, "as compared to other sectors, consumer finance has so far shown a very low level of non-performing loans". The SBP reports that Pakistan's 14 percent share of consumer credit in total private sector credit is still low compared to India, with 24 percent, and Indonesia, with 30 percent.

#### Banking Executives Predict Consumer Financing Rebound

15. (SBU) Banking executives report to local media that they believe the current slowdown in the consumer finance market will rebound once Pakistan becomes more politically stable, inflation is brought under control, and the cost of credit decreases. They note that the consumer credit market in Pakistan still remains very small but has great potential to grow and drive the overall economic development of the country. Since mortgage and auto loans are adequately secured, rising exposure in these areas may not pose serious credit risk to banks, but the high level of unsecured lending - personal

ISLAMABAD 00003104 002 OF 002

loans and credit cards -  
may warrant attention.

Comment

16. (SBU) Until recently, much of the growth in the manufacturing sector, particularly in the manufacturing of automobiles, electronics, and consumer durables, has been led by higher consumer demand spurred on by increased consumer lending. The steep fall in consumer financing growth contributed to a slowdown in many parts of the manufacturing sector in FY07-08. Many economists have questioned the GOP policy of pushing consumption-led growth and have warned of heavy defaults as personal indebtedness and the cost of credit increase; consumer income remains stagnant. With banks becoming more cautious and consumers becoming more reluctant to borrow, demand for consumer financing is likely to continue to decrease. In the current fiscal year, this decreased demand for consumer financing coupled with higher costs of production, could further slow manufacturing growth, which currently stands at 3.7 percent. End Comment.

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